

FISCAL NOTE

Bill #: HB23

Title: Increase cigarette and tobacco products tax

Primary

Sponsor: Rep. Butch Waddill

Status: As Introduced

Sponsor signature	Date	Chuck Swysgood, Budget Director	Date
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Fiscal Summary

	<u>FY2003 Difference</u>	<u>FY2004 Difference</u>	<u>FY2005 Difference</u>
Expenditures:			
General Fund	\$60,046		
Revenue:			
General Fund	\$23,674,348	\$31,891,611	\$31,595,805
Capital Projects Fund (LRBP)	(\$95,006)	(\$127,946)	(\$125,966)
State Special Revenue (DPHHS, Vet. Nursing...)	(\$67,670)	(\$91,132)	(\$89,722)
Net Impact on General Fund Balance:	\$23,614,302	\$31,891,611	\$31,595,805

<u>Yes</u>	<u>No</u>		<u>Yes</u>	<u>No</u>	
	X	Significant Local Gov. Impact	X		Technical Concerns
	X	Included in the Executive Budget	X		Significant Long-Term Impacts
	X	Dedicated Revenue Form Attached	X		Family Impact Form Attached

Fiscal Analysis

ASSUMPTIONS:

- Under current law, the cigarette tax rate is \$0.18 per pack.
- Under this proposal, the cigarette tax rate is increased to \$0.68 per pack beginning October 1, 2002. This proposal is shown in Table 1.
- Under current law, cigarette tax revenues, after tribal revenue sharing payments, are distributed 73.04% to the state general fund; 15.85% to the Long-Range Building Program Account; and 11.11% to the Department of Public Health and Human Services for the operation and maintenance of state veterans' nursing homes.
- Under this proposal, cigarette tax revenues, after tribal revenue sharing payments, are distributed 92.86% to the state general fund; 4.2% to the Long-Range Building Program Account; and 2.94% to the Department of Public Health and Human Services for the operation and maintenance of state veterans' nursing homes. This proposal is shown in Table 1.

Table 1 HB23 (Special Session 2002) As Introduced Current Law and Proposed Law Cigarette Tax Rates and Distribution of Net Revenue		
Revenue Fund	Tax Rate	Distribution of Net Revenue
Current Law		
	\$0.18	
General Fund		73.040%
LRBP		15.850%
DPHHS (Veteran Nursing Homes)		11.110%
Proposed Law - July 1, 2002 to October 1, 2002		
	\$0.18	
General Fund		73.040%
LRBP		15.850%
DPHHS (Veteran Nursing Homes)		11.110%
Proposed Law - October 1, 2002 and on		
	\$0.68	
General Fund		92.860%
LRBP		4.200%
DPHHS (Veteran Nursing Homes)		2.940%

5. Increasing the cigarette tax rate from \$0.18 to \$0.68 per pack will generate new net revenue of \$19,295,439 in fiscal 2003; \$25,985,511 in fiscal 2004; and \$25,583,353 in fiscal 2005. Revenue to the state general fund will **increase** by \$19,458,115 in fiscal 2003; \$26,204,589 in fiscal 2004; and \$25,799,041 in fiscal 2005. Revenue to the Long-Range Building Program Account will **decrease** by \$95,006 in fiscal 2003; \$127,946 in fiscal 2004; and \$125,966 in fiscal 2005. Revenue to the Department of Public Health and Human Services for the operation and maintenance of state veterans' nursing homes will **decrease** by \$67,670 in fiscal 2003; \$91,132 in fiscal 2004; and \$89,722 in fiscal 2005.
6. The impacts in assumption five are calculated using a model developed by the Department of Revenue (DOR). The DOR cigarette tax revenue estimate under current law for fiscal years 2003 through 2005 is used as the base. In addition to DOR's base estimate, a price elasticity of demand for cigarettes of 0.44 is used in this model. The model assumes the price of a pack of cigarettes will increase by the same amount (in dollars) of a tax increase. Given a base cost of \$2.82 per pack, which is used in this model, and an elasticity of 0.44, each penny increase in the price of a pack of cigarettes results in a decrease in demand of 0.16%.
7. Under current law, the tobacco products tax rate is 12.5% of the wholesale price.
8. Under this proposal, the tobacco products tax rate is increased to 50% of the wholesale price beginning October 1, 2002.
9. Under current law and under this bill, tobacco products tax revenues, after tribal revenue sharing payments, are distributed 100% to the state general fund.
10. Increasing the tobacco products tax rate from 12.5% to 50% of the wholesale price will generate new net revenue to the state general fund by \$4,216,233 in FY03; \$5,687,022 in FY04; and \$5,796,764 in FY05.
11. The above impact in assumption ten is calculated using a model developed by the Department of Revenue (DOR). The DOR tobacco products tax revenue estimate under current law for fiscal years 2003 through 2005 is used as the base. In addition to DOR's base estimate, a price elasticity of demand for tobacco products of 0.44 is used in this model. The model assumes a 10% markup from the wholesale list price to the retail price.

(continued)

12. Table 2 shows the summary of the impacts from the cigarette tax increase and the tobacco tax increase under the assumption that there will not be significant stockpiling by the wholesalers or retailers of cigarettes taxed at \$0.18 per pack and tobacco products taxed at 12.5% of wholesale price.

Table 2 HB23 (Special Session 2002) As Introduced Summary of Cigarette and Tobacco Tax Rate Increase Impacts No Stockpiling			
	FY2003	FY2004	FY2005
Cigarette Tax			
Net Revenue			
Revenue - Current Law	\$ 10,630,946	\$ 10,466,419	\$ 10,304,438
Revenue - Proposed Law	\$ 29,926,385	\$ 36,451,929	\$ 35,887,790
Change In Revenue	\$ 19,295,439	\$ 25,985,511	\$ 25,583,353
% Change In Revenue	181.5%	248.3%	248.3%
Change in Revenue			
General Fund	\$ 19,458,115	\$ 26,204,589	\$ 25,799,041
LRBP	\$ (95,006)	\$ (127,946)	\$ (125,966)
DPHHS (Vet. Nursing Homes)	\$ (67,670)	\$ (91,132)	\$ (89,722)
Tobacco Products Tax			
Net Revenue			
Revenue - Current Law	\$ 2,289,516	\$ 2,356,272	\$ 2,401,741
Revenue - Proposed Law	\$ 6,505,749	\$ 8,043,293	\$ 8,198,505
Change In Revenue	\$ 4,216,233	\$ 5,687,022	\$ 5,796,764
% Change In Revenue	184.2%	241.4%	241.4%
Change in Revenue			
General Fund	\$ 4,216,233	\$ 5,687,022	\$ 5,796,764
Impact From Both Taxes			
Net Revenue			
Revenue - Current Law	\$ 12,920,462	\$ 12,822,690	\$ 12,706,178
Revenue - Proposed Law	\$ 36,432,134	\$ 44,495,223	\$ 44,086,295
Change In Revenue	\$ 23,511,672	\$ 31,672,532	\$ 31,380,117
% Change In Revenue	182.0%	247.0%	247.0%
Change in Revenue			
General Fund	\$ 23,674,348	\$ 31,891,611	\$ 31,595,805
LRBP	\$ (95,006)	\$ (127,946)	\$ (125,966)
DPHHS (Vet. Nursing Homes)	\$ (67,670)	\$ (91,132)	\$ (89,722)

13. The Department of Revenue would need 0.50 additional FTE for compliance and administration work in fiscal 2003. Additional expenditures for personal services would be \$16,720 in fiscal 2003. Additional expenditures for operating expenses would be \$1,876 in fiscal 2003. Additional expenditures for equipment would be \$41,450 in fiscal 2003.

(continued)

FISCAL IMPACT:

	<u>FY2003</u> <u>Difference</u>	<u>FY2004</u> <u>Difference</u>	<u>FY2005</u> <u>Difference</u>
FTE	0.50		
<u>Expenditures:</u>			
Personal Services	\$16,720		
Operating Expenses	\$1,876		
Equipment	<u>\$41,450</u>		
TOTAL	\$60,046		

Funding:

General Fund (01)	(\$60,046)
TOTAL	(\$60,046)

Revenues:

General Fund (01)	\$23,674,348	\$31,891,611	\$31,595,805
Capital Projects Fund (LRBP) (02)	(\$95,006)	(\$127,946)	(\$125,966)
State Special Revenue (DPHHS, Vet. Nursing...) (03)	(\$67,670)	(\$91,132)	(\$89,722)

Net Impact to Fund Balance (Revenue minus Expenditure):

General Fund (01)	\$23,614,302	\$31,891,611	\$31,595,805
Capital Projects Fund (LRBP) (02)	(\$95,006)	(\$127,946)	(\$125,966)
State Special Revenue (DPHHS, Vet. Nursing...) (03)	(\$67,670)	(\$91,132)	(\$89,722)

EFFECT ON COUNTY OR OTHER LOCAL REVENUES OR EXPENDITURES:

This proposal has no impact on county or other local government revenues or expenditures.

LONG-RANGE IMPACTS:

Revenue to the state general fund will continue to be greater under this proposal than under current law. Revenue to the Long-Range Building Program Account and the Department of Public Health and Human Services for the operation and maintenance of state veterans' nursing homes will continue to be less than under current law.

TECHNICAL NOTES:

1. The estimates provided in this fiscal note assume there will not be significant stockpiling by the wholesalers or retailers of cigarettes taxed at \$0.18 per pack and tobacco products taxed at 12.5% of wholesale price. The current language of this bill doesn't necessarily prevent wholesalers or retailers from purchasing an unusual amount of cigarettes and tobacco products prior to the tax increase.
2. Table 3 shows the different scenarios for fiscal 2003 if stockpiling occurred. The different scenarios are based on the number of months of stockpiling. The scenarios range from one to six months. *The stockpiling for tobacco products (other than cigarettes) is assumed only to occur for one month in all the scenarios.*

Table 3
HB23 (Special Session 2002) As Introduced
FY2003 Revenue Impacts if Stockpiling Occurs

Description	Stockpiling					
	1 Month	2 Months	3 Months	4 Months	5 Months	6 Months
Cigarette Tax						
Change in Revenue:						
General Fund	\$ 16,948,104	\$ 15,150,525	\$ 13,198,120	\$ 10,497,375	\$ 8,749,007	\$ 6,668,182
LRBP	\$ (82,751)	\$ (73,974)	\$ (64,441)	\$ (51,254)	\$ (42,718)	\$ (32,558)
DPHHS (Vet. Nursing Homes)	\$ (58,941)	\$ (52,689)	\$ (45,899)	\$ (36,507)	\$ (30,427)	\$ (23,190)
Tobacco Tax						
Change in Revenue:						
General Fund	\$ 3,667,405	\$ 3,667,405	\$ 3,667,405	\$ 3,667,405	\$ 3,667,405	\$ 3,667,405
Total Impact From Both Taxes						
Change in Revenue:						
General Fund	\$ 20,615,509	\$ 18,817,930	\$ 16,865,525	\$ 14,164,779	\$ 12,416,412	\$ 10,335,587
LRBP	\$ (82,751)	\$ (73,974)	\$ (64,441)	\$ (51,254)	\$ (42,718)	\$ (32,558)
DPHHS (Vet. Nursing Homes)	\$ (58,941)	\$ (52,689)	\$ (45,899)	\$ (36,507)	\$ (30,427)	\$ (23,190)

3. The Department does not currently have a system for collecting tax past the wholesaler level. Presently, the Department sells tax stamps to the wholesaler who affixes the stamps to the cigarettes. The wholesaler includes the taxes in the price sold to the retailer, who ultimately includes the taxes in the price to the consumer. Assessing the tax increase at the retail level would pose an administrative problem and administrative costs. The costs are provided in assumption thirteen.
4. Section 6 (Applicability) of this proposal is unclear if the current inventory of the wholesaler is taxable under current law or under this proposal.